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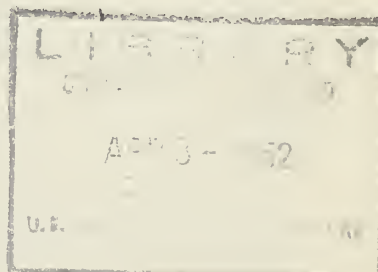
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FINANCIAL PROBLEMS
OF
PURCHASING COOPERATIVES

By

GEORGE J. WAAS



COOPERATIVE RESEARCH AND SERVICE DIVISION

UNITED STATES DEPARTMENT OF AGRICULTURE
FARM CREDIT ADMINISTRATION
WASHINGTON 25, D. C.
I. W. DUGGAN, GOVERNOR

COOPERATIVE RESEARCH AND SERVICE DIVISION

HAROLD HEDGES, CHIEF

JOSEPH G. KNAPP, ASSOCIATE CHIEF

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FOREWORD

This report which was originally presented at a conference of managers from the member associations of Midland Cooperative Wholesale, Minneapolis, reviews some of the fundamentals of sound financing and planning.

While aimed specifically at Midland's operations first and those of purchasing cooperatives second, other types of cooperatives also should find this statement of value.

FINANCIAL PROBLEMS OF PURCHASING COOPERATIVES

By George J. Waas

Senior Agricultural Economist

The balance sheets of many of the local member associations of Midland Cooperative Wholesale clearly show the strain of cash and working capital shortages. Of course I know that you managers do not regard this exactly as a news flash. Now I cannot personally supply the needed capital, nor give you any magic formulas, nor less do I have any new ratios or automatic alarms devised to be either panaceas or warning signals. Rather, I intend simply to refresh your minds on some of the fundamentals of sound financing and planning. To restate these fundamentals might prove of some benefit.

TAXES, INFLATION, EXPANSION

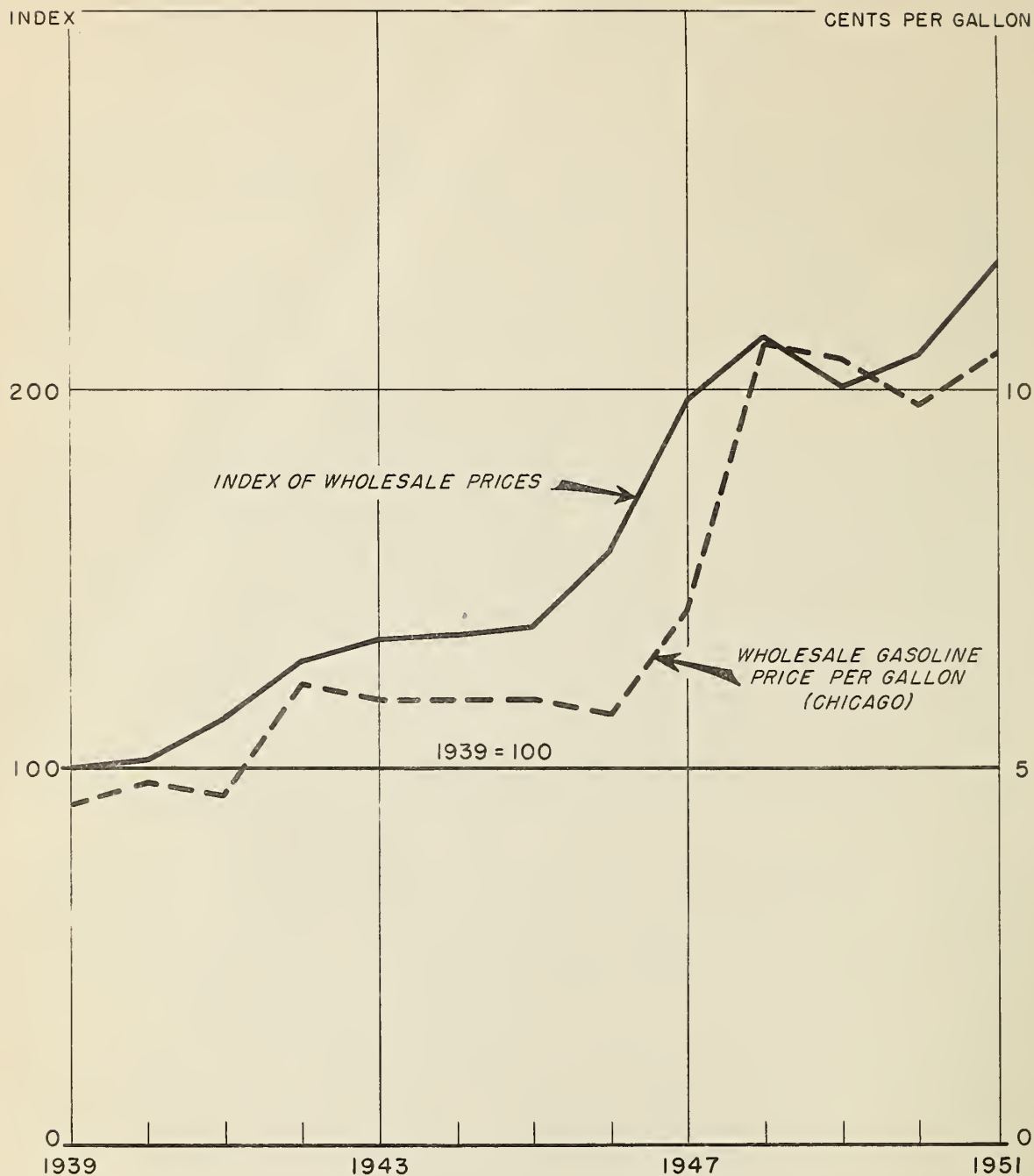
Surely you will join me in the realization that recent outside forces - those beyond the control of management - will tend to cause a further aggravation of capital shortages. First there is the substantial increase recently enacted in the rate of Federal income tax. In the high bracket the corporate rate is now 52 percent, a rise of 5 points or more than 10 percent. This is of compelling interest to all cooperatives, whether they are taxable or "exempt." That word exempt is now in quotation marks since under the new revenue act a cooperative exempt from Federal income taxation is nevertheless subject to that very tax under certain conditions. This sounds paradoxical, but I assure you it is literally true. It is my understanding that more than three-quarters of the 637 member associations of the Midland group were operating subject to Federal income taxation before this latest legislation was passed.

The second influence which has been eating away at your working capital in recent years is the force of inflation. Thus, the capital accumulated in prior years at the old level of the dollar's value, has become less and less adequate to finance inventories, receivables, property acquisitions, and so on, at the higher price levels of recent years.

Figure 1 depicts some of these inflationary factors. The top line traces the rise of 134 percent in the wholesale price index, on a national scale, from the base of 100 in 1939 to 234 in 1951. This gives a rough idea of the increased burden involved in financing the cost of any purchases, including acquisitions of property. For example, a warehouse costing \$100,000 in 1939 would now call for an outlay of nearly a quarter million dollars. Or, as another illustration, an association today would have to secure almost \$250 from each member for every \$100 of capital contributed in 1939 in order to do the same job of financing.

The bottom line in the figure is even of more interest to you as it represents the cost of your principal commodity. It is the price record of a gallon of gasoline as purchased by Midland locals, before taxes and

FIGURE I
PRICE RISES - 1939 TO 1951



	1939	1951	% INCREASE
INDEX OF WHOLESALE PRICES.....	100	234	134
WHOLESALE GASOLINE PRICE PER GALLON...	4.5¢	10.5¢	133
TANK-CAR LOAD OF GASOLINE.....	\$360	\$840	133

freight. The rise of 133 percent is a very close parallel to the other index. This means that if you filled your tanks in 1939 at a cost of say \$2,000, it would take almost \$5,000 to fill them today. Gasoline sales on credit would cause a similar expansion in the dollar volume of accounts receivable.

Therefore, associations which have expanded either through an increase in the number of units sold, by adding new lines of goods, or by the purchase of improved facilities -- all normally to be considered as marks of success -- have been, in late years, fighting an unequal battle with taxes and inflation. This is especially true if they have been redeeming capital stock and making heavy cash payments of patronage refunds and dividends on capital stock.

INADEQUATE CAPITAL INCREASES

Your capital, indeed, may have actually increased in this period, both from direct and indirect contributions made by member-patrons, but the sad truth is that the increases in many instances have not kept pace with the upsurge in the course of inflation and expansion.

A considerable number of associations are now pinched for cash even though their net working capital has risen somewhat in recent years. Cash was crowded out of the picture, with receivables and inventories swollen not only by higher price levels, but also by true increases in business volume, along with an increasing laxity in the collection of receivables.

The ratio of cash to current liabilities in one case dropped in a few years from 2 times to less than one-half of one time. Of course, it is admitted that receivables and inventories can be pledged to secure loans from banks, but it is more desirable, ordinarily, to use owned capital for permanent or semipermanent expansion. In short-term peak periods bank-loan financing is probably more to be desired than the use of equity capital.

Whether the war situation will get hotter or colder, how long it will drag out, and its effect upon the continuance of our present system of flexible price controls, are matters on which I will venture no prediction. It is understood, however, that most of the goods handled by Midland associations are under some form of price control that generally allows the possibility of moderate price increases. If price increases should become necessary, are you prepared for them? Are you conserving capital now in anticipation of such an event, or to cure present capital shortages?

CAPITAL SOURCES, EXPANSION, CONSERVATION, REVAMPING

Now what can supply associations do to conserve capital, or to increase it? May I direct your attention for a moment to figure 2 on which are listed the five principal sources of cooperative capital? The sixth

Figure 2. - *Main sources of capital for supply cooperatives.*

1. OUTSIDE INVESTORS	(a) In capital stock (b) In bonds or notes (c) By reduction of dividends on shares and postponement of share redemption
2. OWNER- PATRONS*	-----Direct Contributions----- (a) In capital stock (b) In bonds, notes or unsecured loans (c) In equity certificates
3. OWNER- PATRONS	-----Indirect Contributions----- (a) By issuance of noncash patronage refunds (b) By reduction of dividends on shares and postponement of share redemption
4. CREDIT GRANTORS	(a) Commercial banks (b) Banks for cooperatives (c) Regional cooperatives, etc.
5. OPERATING EFFICIENCY	(a) Increased sales volume (units) (b) Increased purchasing skill (c) Lowered operating costs (d) Lowered interest costs from rearrangement of capital structure, elimination of slow-moving products, etc. (e) Lowered taxes by change of tax status
6. INTERNAL TRANSFERS	-----Not Actually Sources----- (a) Reduction of receivables and inventories (b) Sale of property no longer needed (c) Depreciation charges

*Group 2 items may or may not be linked to patronage volume.

item is not a true source, but is rather a transfer of capital from one section of the balance sheet to another, such as the increase of cash from the reduction of receivables and inventories, from the sale of property, and the like.

A brief examination of each of these sources of capital, along with possible rearrangements of capital structure, should enable you to appraise the chances for improving your own association's financial position.

CAPITAL FROM OUTSIDE INVESTORS

Source number one concerns the possibility of securing capital from outside investors. In the case of local associations we might as well check that one off as a virtual dud. Although in some areas associations have managed to interest the public in preferred stock, I understand Midland locals has sold very little stock to outsiders. Some forward-looking cooperative leaders have in mind the possibility of developing a special exchange for trading in the securities of cooperative organizations. Whether or not this idea will prove compatible with the present-day concepts of control by producers is a matter for some further research.

I want to leave only one thought with you as to this first source of capital. Do you feel that the utmost has been done to tap this group of investors? Frankly, on the local association level, I am not optimistic about the possibilities. Investments good enough to attract the local public might also have to carry a high financing cost in interest or dividends.

CAPITAL FROM PATRONS -- DIRECT AND INDIRECT CONTRIBUTIONS

Next is item 2, direct contributions from patrons. Even though farmers have been quite prosperous for a number of years, the current high tax rate might prove to be a deterring factor in efforts to secure direct help from them. But are we sure of this? Would a strong campaign of promotion and education coax some funds out of the piggy banks that must be tucked away somewhere? Of course, your members would have to be fully convinced of the organization's vital need for funds and of the soundness of any projected expansion. Perhaps some dramatic factor like the survival of the association or curtailment of its services might prove a motivating force.

Undoubtedly some of you are thinking "Oh poppycock, you couldn't get a thin dime out of our members now under any circumstances." Alright, I don't intend to argue on that score. All I mean to say is that if direct funds can be secured from members at all, it probably can be done best by a careful program of education and planning.

A survey recently conducted by Dr. E. Fred Koller, of the University of Minnesota staff, showed that in Minnesota at the end of the fiscal year

1949-50 local farmers' cooperatives owed to individuals almost 27 percent of their total borrowings. It is probable that most, or perhaps virtually all, of these lenders were association members or former members rather than outside investors. The proportion, however, secured from individuals is surprisingly high and indicates that this is a significant source of capital that should not be overlooked in financial planning.

And now let us leave the first two sources and tackle one that offers the greatest possibilities because it is the heart and lifeblood of successful cooperation. I refer to item 3, indirect contributions from owner-patrons. These may arise from the issuance of patronage refunds in capital stock or other noncash forms, or through the reduction or elimination of dividends on capital shares and similar sources.

Often cooperative managers say that members are not willing to make sufficient capital contributions of either direct or indirect types. Can this mean that the members are not aware of the protection, benefits and privileges they secure through the operation of their cooperative? Or are they so blindly selfish as to want these things without extending themselves to pay for them? Is it really a case of wanting their cake and eating it, too?

There has been far too much of this somewhat rebellious attitude which submerges, usually in an aura of mystery and some suspicion, what is essentially a very simple situation. The simplicity lies in the truism that if members want to have something of value they must assist in paying for it. If it is taking longer to pay for than they deem reasonable, a little inquiry might provide satisfactory answers and remove the iron curtain of misunderstandings.

Some of the answers have already been discussed, such as the epidemic of inflation, the tumors of natural growth, and the swellings resulting from extra expansions like ventures into new lines, or into vertical integration involving the internal production or processing of materials formerly purchased. The latter phases are applicable, of course, mainly to the central organization, but the locals primarily finance the central.

EXPANSION DIFFICULTIES AND DANGERS

While expansion of these types is normally to be greatly desired, in these days it could turn out to be virtually a two-edged sword capable of plunging an association into disastrous failure if done without an adequate or commensurate increase in owned capital -- or, as a secondary alternative, in funded long-term debt owing to members, with the third alternative being funded debt owing to outsiders.

One rule that should be put down in the management's little black book in the No. 1 position is never to undertake any act of expansion, large

or small, without the enthusiastic approval of a strong majority of the membership, including their expression of willingness to make direct or indirect contributions of capital to safely finance the undertaking.

Rule No. 2: Always get as much outside help as possible from trained technicians like engineers and financial counsellors - even if it costs a little - in arriving at decisions involving expansion. Remember, you might be too close to the forest to see the trees!

Rule No. 3 might be to take the conservative approach always by depending less on a forecast of expected operating funds from the new facilities and more on direct financial help from your members. In other words, have a realistic, adequate plan that does not rely upon some intangible, mysterious source to make up a deficiency in capital.

The last of the expansion rules is No. 4: Don't stub your toes by expecting to spend only the basic construction cost of a new building without at the same time realizing that the anticipated increase in business will require perhaps some considerable increase in working capital for new receivables, inventories, payroll, and the like.

It is clear that the membership has the right, if it chooses, to be satisfied with a small business and small refunds, versus the responsibility of capitalizing an expansion of the present organization. If this is the case the management and directors must accede to any such decision and abandon their hopes for a larger organization until such time as they can convince the members of the merits of their plans.

CONSERVING CAPITAL

Returning to item 3 on figure 2, indirect contributions from member-patrons. There are many cases where cooperatives have gotten into serious trouble by going hog-wild on the payment of cash refunds and dividends on capital stock. Good managers and directors, with some selling ability and ingenuity, should always be able to convince their members of the futility of these practices. By all means cut these cash payments down before it is too late to rescue your good organization. I don't have to suggest what is a desirable percentage to retain. This will vary. Look at the facts, look at the dollars, use horse sense and decide on your own recommendation to the membership. But decide in a way which favors the positive survival of the association.

Now as to dividends on capital stock. Where the stock was issued for patronage refunds you should not hesitate to cut out the dividend payments, if your association needs capital. But if the stock came from direct sale you probably will not want to consider a stoppage of dividends except as a last, emergency resort. You might, however, give some thought to a reduction in the rate as a less serious blow to the investors.

Cooperatives have a way of building up a tremendous pride over the payment of regular dividends on capital. All well and good when you can

afford it! A continuation, however, of payments by an association pinched for capital becomes merely the exercise of false pride, something which should be definitely curbed.

Another closely related point is the saving of funds possible from passing or postponing the redemption of capital shares. In this North Central section there seems to be a kind of fervor, almost like a religion, that impels cooperatives to immediately redeem capital shares when a member dies or moves away from the locality. The yearly amounts of such redemptions in the case of several associations have been amazingly large.

Actually these redemptions are made without any legal obligation to do so. It is a voluntarily assumed burden stemming entirely from moral or ethical grounds. Again this is fine and noble, but only when you can afford it. Right at this moment this practice is causing serious embarrassment to a number of long-established, substantial cooperatives. They actually are being unconsciously liquidated.

Whenever possible, of course, some preference should be given to share redemptions in the case of deaths. This follows from the fact that many members no doubt count upon these redemptions as a protection for their families in much the same way as they look upon the proceeds of a life insurance policy.

It might be of interest to realize that in most sections of the country cooperatives do not show the same solicitude toward lost members, even when the organization can afford to make the payments. Usually the withdrawing member simply takes his regular turn on redemptions brought about by revolving of the capital. Managers, get your directors to join you in making a study of this situation, particularly as to its effect on your financial position.

CAPITAL FROM CREDIT INSTITUTIONS AND OTHERS

The fourth group on figure 2 covers loans from banks and other cooperatives. You know the possibilities in that direction as well or better than I. A desirable goal for any business, but one almost never achieved, is to finance operations entirely from equity capital. Many argue that the needs of seasonal peaks are better financed by banks. Certainly this is true whenever the bank interest rate is lower than the dividend rate on capital stock, or the interest charges on notes owing to members.

Dr. Hutzler Metzger, president of the St. Paul Bank for Cooperatives, has already given you his views on the procurement of loan funds from banking institutions at this conference. Because of this I shall make no attempt to discuss this subject here in any detail.

CAPITAL FROM OPERATING EFFICIENCY

The fifth source of funds includes what might be called the sponge-squeezing items. Here we look to managerial ability to promote increased

sales volume and to achieve reductions in operating costs. Here we look for improved operating methods and plant lay-outs leading to better utilization of materials and labor.

There might be a tendency sometimes to lose sight of the fact that cooperatives fundamentally should not be as much concerned with sales prices and mark-ups as their competitors. The cooperative's aim is to operate ultimately at cost for the benefit of its patrons. Thus, the very greatest achievement of cooperation in the purchasing field should be in reducing the costs of purchasing, processing, handling and distribution. I am, of course, fully conscious that supply cooperatives employ a useful device when they match the prices of competitors and then prove the worth of their services to members by the amount of residual operating proceeds (net margins).

Of course, it need not be emphasized in this gathering that the whole monetary value of a cooperative cannot be reckoned merely by the amount or rate of its net proceeds since many cooperatives exert a considerable influence on the pricing policies of their competitors. Aside from that, you and I are also keenly aware that the true and final worth of cooperation is not to be measured in dollars and cents alone. Cooperative members have collateral satisfactions such as the pride and responsibility of self-help and self-ownership, the sense of working shoulder-to-shoulder with fellow farmers in a concerted effort, the greater availability of marketing information, and a stronger voice in the selection and quality of farm supply items.

REVAMPING OF CAPITAL STRUCTURE

Another class of cost reductions, but one which the employed management cannot put into effect without the consent of the members, is the possible rearrangement of the capital structure so as to reduce the outlay for interest, dividends, and possibly taxes. At the moment this field seems to offer some opportunity for increased conservation of capital. Therefore I want to go into this in some detail to present a specific plan of action.

Figure 3 depicts a balance sheet with a capital structure often found among local purchasing associations. Looking first at the left-hand column let us assume that this association for many years has taken pride in its constant annual payment of 4 percent on the capital stock of \$400,000. Assume further that the association is suffering from growing pains and inflation which have caused a pinched working capital position, a current ratio of less than 2 times, and a real shortage of cash.

You will note the association has an unusually high rate of ownership equity - almost 90 percent - which it has maintained for years. But it has drained its capital to pay the annual dividends. These figures are based upon the actual experience of one local supply cooperative. Its solution to the problem is ingenious and I want to bring it to your attention with some emphasis.

Figure 3. - Balance sheet of sample association before and after capital rearrangement

<u>Before</u>	(000 OMITTED)	<u>After</u>
<u>\$497</u>	Total Assets.....	<u>\$497</u>
	LIABILITIES	
	Current Liabilities:	
	Payables:	
\$ 35	Trade Accounts Receivable, Notes, Etc.....	\$ 35
<u>25</u>	Taxes and Dividends.....	<u>25</u>
<u>\$ 60</u>	Total Current Liabilities.....	<u>\$ 60</u>
	Fixed Liabilities:	
<u>0</u>	Subordinated Debenture Notes Due Members at 4%.....	<u>\$200</u>
	CAPITAL EQUITIES	
	Capital Stock:	
\$400	Common.....	\$200
<u>12</u>	Share Credits.....	<u>12</u>
<u>\$412</u>	Total.....	<u>\$212</u>
<u>25</u>	General Reserve.....	<u>25</u>
<u>\$437</u>	Total Capital Equities.....	<u>\$237</u>
	LIABILITIES & CAPITAL EQUITIES	
<u>\$497</u>	Total.....	<u>\$497</u>

Its capital stock was all common and had been secured from two sources. Analysis showed that roughly one-half of it arose from direct cash subscription from members. In a special meeting of the members it was agreed that this half of the stock would be converted into unsecured debenture notes carrying 4 percent interest.

In making a switch of this type it must be taken into consideration that those necessary evils, the bankers, undoubtedly will cast a negative eye on the whole procedure unless two important factors are properly covered. First, the notes must be not only unsecured, but must be subordinated to other creditors, certainly at least to any bank loans.

Second, the longest due date possible should be applied to the notes. If you insist on pinning me down for a specific duration, I'll have to say follow what some of our largest corporations have done with their bonds - issue them for 99 years. Perhaps the best way to decide on a period is to call in your banker and ask his opinion of your views.

A long maturity date provides a flexible arrangement since redemptions can be made at any time prior to maturity. Whether the notes are sold for cash, or are converted from patronage refunds, it would be possible to arrange a system of serial (revolving) redemptions, if desired.

So, looking at figure 3 again, we find in the right-hand column that the shift of \$200,000 is indicated. Even with a long-term due date the notes are technically liabilities, yet in another sense they lose none of their attributes as equity capital. (It is possible, however, that you might be able to reach the Minnesota 50 percent reserve requirement faster because of this shift.) The balance of the stock, or another \$200,000, arose through issuance of patronage refunds. This balance was left intact as stock but with the understanding that the association would be forced to suspend payment of dividends thereon until its financial condition improved.

By this rearrangement the association (which was subject to Federal and State income taxes) was able to reduce the drain on its capital outlay by \$28,000 annually, calculated as follows:

Former annual outlay:

To provide for dividends on capital stock	
and income tax applicable thereto-----	\$32,000
(Income tax on next above--at say 50%-----	\$16,000)
(Remainder paid as 4% dividend on stock-----	<u>16,000)</u>

New annual outlay:

4% interest on debenture notes-----	\$8,000
Less: Income tax deduction therefor (50%)-----	<u>4,000</u>

Total -----	<u>4,000</u>
(Reduces effective interest rate on notes from 4% to 2%)	

Reduction in annual outlay----- \$28,000

Managers of taxable cooperatives will want to look into a shift of this type, particularly when it is realized that capital is conserved to the extent of \$28,000 annually, against an immediate effective reduction to members of only \$8,000 of investment income (the difference between dividends of \$16,000 and interest of \$8,000).

Of course, in the long run the members get credit for the entire \$28,000. In fact they have an immediate indirect benefit arising from the association's improved financial standing and its consequent ability to serve its members better. It must be understood that if the association is to be free of income tax on the \$28,000, the amount must be allocated among the members, following which each member reports his share for individual income taxation. In most instances, however, the member's tax will be quite small.

I was asked whether such a revision in the capital structure is entirely ethical from a tax viewpoint. So far as my knowledge extends, the

answer is yes. There have been a number of tax court cases where close corporations were debarred from making an interest deduction for notes or bonds converted from capital stock. I cannot see, however, that the cooperative situation is analogous to those cases.

Bear in mind that two major requirements must be properly covered. First, the notes must have a definite maturity date however long, and second, the payment of interest must be mandatory at stated times, not optional. The absence of either one of those factors undoubtedly will cause the taxing authorities to view the notes as a disguised form of capital stock and accordingly they will disallow the interest as a deduction from taxable income in the case of nonexempt cooperatives.

CHANGE OF TAX STATUS

The revenue act of 1951 which became law recently amends the Internal Revenue Code by adding thereto a new section (101(12)(B)) providing that the presently exempt farmers' marketing and purchasing associations shall become subject to Federal income tax on any savings not allocated and disclosed to patrons, or not paid out as dividends on capital stock.

Some cooperatives in the past have deliberately chosen a nonexempt status because they did not wish to avail themselves of the privileges of full exemption. Associations in that class, which can qualify under the new section of the Code, may wish to review the possibility of benefits from a change in their tax position.

CAPITAL FROM INTERNAL TRANSFERS

Collection of Receivables

In the sixth group of figure 2, covering internal transfers of capital, your attention is directed to the reduction of receivables from the viewpoint of credit policy and firm collection methods. First, it probably will have to be assumed that credit to patrons is a must because that is your competitors' policy. Now this assumption is made rather reluctantly because many cooperatives have been eminently successful without extending a penny of credit. But to avoid argument, let it be granted that in the petroleum business you must match your competitors. By all means, however, stop matching them when it carries your credit policy to the point of becoming unduly liberal and unsafe.

Among your local associations there appears to be little difference in the rules for extending credit to patrons. Usually it is a maximum of 30 days, or one tankful of gasoline. However, there is a rather wide variance in the way these rules are being enforced. This is borne out by the fact that, in the case of sizable oil associations, the turnover rate of receivables ranges all the way from 3 days of sales, to over 49. (Some analysts prefer to call this the collection ratio, or the average collection period.)

A lax credit policy has a tendency to compound itself, to become worse in a sort of algebraic progression. Members seem to work up a strong resistance to a firmer policy. But some climactic event always arises which can be used as an incentive to go out and put on a vigorous collection campaign. It might be that you must have funds to construct a new building, or for some other equally pressing purpose. When you once whittle the accounts down, then is the time to start fresh with a new, firmer credit policy. A few crackdowns in the form of judgments will show that you mean business and the news will spread around quickly.

Managers should pay close attention to the collection ratios and the age analyses of receivables which are being so efficiently furnished to them by the auditors. Directors should consider the possibility of giving the auditors more responsibility in the direction of inspecting and appraising the receivables periodically to determine their collectibility. This might furnish the basis for the set-up of more realistic reserves for doubtful accounts.

Since the collection ratio has been growing progressively worse in recent years; the question of excessive credit must be regarded as a major problem, yes a major hazard, among your local associations. If your organization is in the slow turnover group, consult with some of the other managers here and find out what formula they use for faster turnovers without aggravating or losing members. Remember the catchy song: "Anything you can do, I can do better." Remember, also, that business in general has the practice of tightening credit policies in periods of prosperity, and softening them during depressions. You are apparently engaged in reversing that good rule.

Consideration might also be given to the possibility of unifying the credit policy among all associations, if that is feasible. This might give the policy a backbone or talking point it otherwise would lack.

Top-Heavy Inventories

Getting back to item 6-a again on figure 2, let us go briefly into the matter of inventory problems. First about the records. Do you have an adequate system of perpetual inventorying to aid in the proper planning of purchases so that you will meet the needs of patrons without over-buying? Are you on the ball when it comes to the timely disposition of old, obsolete, shopworn, or discontinued lines of merchandise? Or do you have a lot of such junk on hand counted at cost when its actual market value may be much less?

The inventory turnover - by which I mean the number of times the average inventory value can be divided into the annual sales (or, better, cost of sales) - has in recent years been running unfavorably and abnormally low for many of your local associations against the pattern of prior years. The general indication is that stocks have been carried in excess of needs, probably resulting from poor control of purchases, or careless estimates of sales demands.

Your auditing service recently made the comment that the numerous warehouses built in recent years apparently are being used as storage depots rather than as feeders for current sales. Thus to have ample space -- usually considered a God-send -- might actually have the boomerang effect of encouraging overbuying and of taking on slow-moving lines of merchandise which may be more trouble than they are worth considering their drain on working capital and the cost of their financing.

Of course, I am not unmindful of the possibility that some overbuying in the last year or so probably was actuated by a desire to stock up on items that might become unobtainable under the war production economy. We will have to assume this is a wise course unless it throws your working capital into a tail spin.

Another hazard of excess inventories lies in the greater losses possible in case of a price drop. Did you ever think about the incongruity of an economy that is preoccupied with price ceilings but not at all interested in floors? The younger generation of today can hardly conceive of price declines, but you and I know they are in the picture still, at least in cyclical spurts.

There is a silver lining to the cloud of excess inventories in that any gain on price rises will be correspondingly augmented. (Naturally I refer only to price rises that are permissible under the price control system.) No doubt some managers take this into consideration. In normal times it is often possible to make large gains from inventory price increases and there have been terrific temptations in the past to take a flyer in that direction. It is quite a delicate question. But I would say that in a cooperative operation no speculation should be countenanced.

As in the case of top-heavy receivables, already discussed, those associations afflicted with excess inventories would do well to have their managers learn how other associations have achieved a mastery of the problem. In some instances slow turnovers will not actually be the result of overstocking, but may arise from a higher proportion of slow-moving items. Thus, for proper analysis, inventory turnover should not be viewed on an overall basis, but a separate turnover figure should be calculated for each group of products having similar characteristics or features.

For example, consider an association which just recently added farm machinery and parts to its line of products. Those items, as you know, will knock the overall turnover rate for a loop. Considerable capital can be tied up in display pieces alone, not to speak of the large variety of parts that often must be carried. The managers who are on top of the turnover problem can give you many more constructive and practical suggestions on how to solve it than I can.

Other Capital Transfers

Item 6-b on figure 2 is self-explanatory. Amounts received from the sale of fixed assets are sources of working capital, yet they do not increase general capital unless a gain is made on the sale. It is interesting to realize that the amount of depreciation charged to operations represents in effect a conversion of fixed assets to current assets, virtually identical with the effect of a sale of fixed assets.

Depreciation, in one sense, becomes a sale of property to the customers or patrons. When a business is favorably operated the depreciation is actually collected from customers in the sales price and thus finds its way into the working capital as cash or cash equivalent. Of course, it is necessary to add that the cash from depreciation disappears from working capital as it becomes necessary to replace fixed assets or to purchase additions thereto.

Net margins, as such, do not appear on figure 2 for the technical reason that in a cooperative operation the margins at all times are the property of patrons. Thus, only the amount authorized by the members to be retained by the association as deferred patronage dividends, including conversions thereof to capital stock or reserves, are true sources of capital. The other portion of net margins comes in and goes out of the business almost simultaneously in the form of cash refunds.

THREE GREAT DANGERS

Hans Lahti, manager of the Cooperative Auditing Service at Minneapolis, and one of the most astute analysts of cooperative operations in this country, recently expressed the belief that excess receivables and inventories are the two major defects among supply cooperatives in this section. I second his conclusion and add my own emphatic warning that steps should be immediately taken to remedy these defects, along with some necessary curbs on overexpansion in the acquisition of real property.

Diversification of products handled, including the addition of slow-moving lines, is normally a desirable development, as stated at least once previously. But in times of inflation this often demands heavier additions to equity capital for the financing of inventories and fixed assets than most associations can reasonably secure. Thus, you are caught between the devil and the deep blue sea. I am a little afraid to speak out too sharply against diversification and expansion because the sales department people might believe I am interfering with their plans.

To re-emphasize the hazardous trend in credit I want to add that for a large group of oil associations there is shown an average of over 30 percent more in the closing 1951 receivables, than for the previous year. This cannot be attributed in any large degree to price rises since the average sales volume increased only 4 percent and gallonage of light oils actually decreased nearly 2%. The heavy rise in outstanding

accounts can only be regarded as alarming. It is likely that closing inventories also showed a similar increase, although no aggregated figures on this appear to be available.

So much for the sources, conservation and revamping of capital.

FINANCIAL RATIOS AND CAPITAL MANAGEMENT

Any discussion of financial management would not be at all complete without some consideration of the meaning and effective use of formulas, ratios, and indexes. Generally I try to avoid dealing with specific goals in ratios before I have had a chance to analyze the condition of a particular business.

One of the important features about ratios and indexes is knowing when not to be guided by them. Of course, I have reference here to general rules and ratios that do not fit the particular industry in which one is interested. Is there any point, for example, in an oil association being concerned over the fact that grocery chain stores have very fast inventory turnovers? Recently one was reported to have a turnover oftener than once a week.

Now you are fortunate in not having to explore all of these unrelated statistics. You can refer to a tabulation made for almost two decades covering ratios logically grouped by different classes of your own associations. Because of this long background it is assumed that all or most of Midland's managers are generally familiar with ratio techniques. This discussion accordingly, will be directed away from the elementary phases.

The fine statistics which are available to you represent a veritable gold-mine of information and inspiration. They should inspire the weaker associations to improve their efficiency, while the stronger ones have an incentive to hold on to their leadership. Great credit should be given to your auditing service for the development of this extremely valuable information.

But even though you have what appear to be solid and accurate comparisons among similar businesses, ratios should not even here be taken as inviolable standards or indicators without much in the way of supplemental, comparative analysis. For instance, to determine the real underlying reasons for performance differences between any two associations might take a lot of digging.

Often it will be impossible to make such analyses because the two associations may not be willing to reveal certain facts that would show up one as more efficient than the other. The curtain of competitive secrecy has been admirably drawn aside to a degree among your associations, but it is likely that some limits exist in the area of disclosure.

Probably one of the best ways to use the statistics compiled for your associations is to separate each ratio first into brackets of business-volume groups. Then in turn each such bracket may be divided into three

groups of one-third each, namely the best third, the median third, and the least favorable third. In each group would be shown the high figure, the median, the low, and the average. Each association could then classify its own standing for each ratio within one of the three groups. It might then inquire into the reasons for any poor showing following which efforts could be made to improve its performance, if possible.

So far I have generalized; I will now try to be at least a little more specific.

BALANCE SHEET MEASUREMENTS

The Current Ratio

Perhaps the best known test of financial condition is the current ratio, that is, the relationship of current assets to current liabilities. It is a supplementary gauge to the working capital position that is of primary interest to banks and other short-term creditors, as well as to internal officers.

As with some other things we have a somewhat paradoxical situation with respect to this ratio. If the ratio is good and high and there is plenty of cash, one, of course, has no need for help from a bank. Yet the banks shrink from making a loan on a low ratio although this is the very time one would most need a loan. Now I don't mean this too seriously because a bank should be willing to lend you at least some proportion of the receivables and inventories, if not the property assets, when they are given as security.

What is a desirable current ratio? No doubt you know that this varies between types and sizes of business, seasons of the year, differing credit policies and the relative price level of the products handled. In the case of your supply cooperatives I understand that at low inventory time, usually at the close of the fiscal year, a ratio of 3 to 1 is considered generally satisfactory. It is, of course, desirable to set a goal higher than that.

A large group of your oil associations averaged about 2 1/2 times in 1950. This dropped to 2 1/4 in 1951, a rather bad trend. Since the average includes many organizations with very low ratios, the standing of your own association can best be judged by comparison with the upper third, as already outlined.

There is nothing divine about the choice of a desirable ratio. This can be illustrated by a story about the origin of the much used 2 to 1 figure. It seems that bankers many years ago thought this up as a minimum because they theorized the current assets could not within reason shrink more than one-half. There are really many people who regard an estimate as more valuable when it is based upon another estimate.

There's one point I want to comment on particularly. The current ratio, as a supplemental index of working capital condition, almost never

should be taken alone. Rather, it must be considered in conjunction with the liquidity characteristics of the current assets, and the due dates of the current liabilities. Thus, a ratio of 4 to 1, with a low proportion of cash and other quick-liquid items, may not be as favorable as a 2 to 1 ratio where the liquidity factor was outstandingly good.

Several other ratios have the same characteristic in that they should not be regarded alone but rather in association with one or more other related indexes. In still other cases ratios will be found valuable as a trend indicator, rather than as an exact measurement at any particular moment.

Liquidity Ratios

An effective index of liquidity is the quick asset ratio, sometimes called the acid test. This measures the relationship between current liabilities and current assets, exclusive of inventories, the latter normally being considered as having the least liquidity among the group. A minimum of 1 to 1 in this ratio is considered good, as a general rule.

Of very similar significance is the ratio of current liabilities to the inventory. This indicates to the creditors how much reliance they have to place on inventories in the redemption of liabilities owing to them.

Another ratio in the same class considers the amount of cash as related to the total of current liabilities (by dividing the former by the latter). Anything approaching one, or higher, normally would be considered a desirable figure. This ratio might be easier to understand if it were stated as a percentage of the current liabilities. Thus, for example, cash would be stated simply as equal to say 50 percent of the current liabilities, rather than using the ratio of .5 to 1.

Net Working Capital

We come now to a very well known standard for judging financial stability, the amount of net working capital, or the excess of current assets over current liabilities. Almost everyone knows that the larger this excess, the better off is the business. But the true nature and function of this capital fund is perhaps not well enough known. Is it realized, for example, that this fund is sensitive to almost every transaction, being influenced upward or downward by changes in fixed assets, liabilities, equity capital, and by the flow of net operating proceeds or operating losses sustained? It is very much like the main artery in a person's heart.

Of course, anyone familiar with the application of funds statement now in general use by accountants, knows all of this and more. Greater attention should be given to this particular statement (see figure 4, for example) as a working tool by managers. It unfolds a story of financial developments almost as useful as the operating statement and balance sheet.

Figure 4. - Sample associations Nos. 1 and 2 - capital sources and uses for the 13 years 1939-1951

Assoc. No. 1 <u>Actual</u>	(000 OMITTED)	Assoc. No. 2		
		Actual	Desirable	
			Changes	Final
	<u>CAPITAL SOURCES</u>			
\$ 701	Net Margins (Before Depreciation; After Taxes).....	\$ 607	-	\$ 607
	Issuances of Capital Stock:			
74	For Cash Sale to Members.....	111	-	111
352	For Patronage Dividends.....	234	+\$150	384
0	Sale of Physical Properties.....	9	-	9
29	Mortgage Loans.....	45	-28	17
<u>\$1,156</u>	<u>Total Capital Sources.....</u>	<u>\$1,006</u>	<u>+\$122</u>	<u>\$1,128</u>
	<u>USES OF CAPITAL</u>			
\$ 186	Increase in Net Working Capital.....	\$ 102	+\$122	\$ 224
	Outlays to Members:			
72	Dividends on Capital Stock.....	47	-	47
58	Patronage Dividends Paid in Cash.....	207	-150	57
352	Patronage Dividends Paid in Capital.....	234	+150	384
24	Redemption of Capital Stock.....	70	-	70
288	Acquisition of Physical Property or Equipment.....	191	-	191
176	Investment in Regional Cooperative (And Others).....	155	-	155
<u>\$1,156</u>	<u>Total Uses of Capital.....</u>	<u>\$1,006</u>	<u>+\$122</u>	<u>\$1,128</u>

Previously I pointed out that even where net working capital has shown an increase, the association's position actually may be getting worse if the increase is inadequate or is tied up mainly in receivables and inventories. You can't pay liabilities with these noncash items before they are liquidated. You can get a bank loan on them, of course, but then you have merely exchanged one liability for another if the loan is used to pay off other creditors.

Working Capital Management

Reference to figure 4, showing the in-and-out flow of capital, will illustrate good and bad examples of capital management, and how ratios

measure the result. Incidentally all of the figures shown to you today are based on actual records of supply associations similar to your locals.

On the left part of figure 4 are listed the capital transactions for an association with a good performance, during the inflationary period of the last 13 years. Note how well it did in securing cash capital from members through sale of stock and conversion from patronage refunds. It did pay out \$72,000 - quite a sizable chunk - for dividends on capital stock, but the important point is that it could be afforded. On the other hand, it conserved capital greatly by going light on the payment of cash refunds, only \$58,000 being so involved. Similarly, its \$24,000 redemption of capital stock was modest.

For convenient illustration, I have shown the conversion of margins to capital stock, amounting to \$352,000, in both the upper and lower sections of the statement, even though this causes a duplication of the net margin source.

Now this association is a go-getter and it had no intention of being left behind in the expansion parade. So it purchased new buildings and equipment to the tune of \$288,000, and also added \$176,000 to its investment in the regional. The latter really represents a share in each of the assets owned by the regional, whether it be working capital, buildings, oil refineries, or whatever. But, again, the association could afford all this expansion because it received ample new capital and conserved its cash outlays for patronage refunds. All of this resulted in a healthy increase of \$186,000 in net working capital, bringing the current ratio up to 4 times, with cash constituting more than 5 percent of the current assets. And so this association lived happily ever after.

Turning now to the weak association, No. 2, shown on the right-hand side of figure 4: This organization had a sales volume very similar to that of association No. 1. But it went overboard on cash outlays to member-patrons which totaled \$324,000 in dividends and stock redemptions. It also indulged in heavy expansion of physical property to the amount of \$191,000. The increase of \$102,000 in net working capital was inadequate to take care of its increased liabilities. The closing current ratio was low with a slim margin of cash. You can see only one bright spot and that is the cash sale of \$111,000 in stock to members. If it were not for that, no increase would have occurred at all in net current assets.

Let us see what association No. 2 could have done to improve its position. We shall use hindsight here as a sort of medicine for curing future afflictions. With only one stroke this association could have entirely changed its financial picture. If they had shifted \$150,000 from a cash refund to a capital stock refund, this would have permitted a pay-down of \$28,000 on mortgage loans, with a consequent saving in interest. It would also have brought their net working capital up to \$224,000 with a high current ratio.

On the supplemental figure 5 is shown a condensed balance sheet for association No. 2 before and after the changes just discussed. You will notice that the old current ratio of 1.8 was increased to 6.2. The fund of \$150,000 was used to retire a portion of both current and fixed liabilities. This increased net working capital by \$122,000 and put the association on easy street.

Figure 5. - Balance sheet - 1951 actual vs. desirable - for sample association No. 2

Actual	(000 OMITTED)	Desirable	
		Changes	Final
	ASSETS		
\$312	Current Assets.....	-	\$312
171	Investments.....	-	171
145	Fixed Assets - Net.....	-	145
\$628	Total Assets.....	-	\$628
	LIABILITIES		
\$172	Current Liabilities.....	-\$122	\$50
44	Fixed Liabilities.....	-28	16
\$216	Total Liabilities.....	-\$150	\$66
	CAPITAL EQUITIES		
\$310	Capital Stock and Credits.....	+\$150	\$460
102	General Reserve.....	-	102
\$412	Total Capital Equities.....	+\$150	\$562
	LIABILITIES AND CAPITAL EQUITIES		
\$628	Total.....	-	\$628
\$140	Net Working Capital.....	+\$122	\$262
1.8	Current Ratio.....	+4.4	6.2

Ownership Ratios

Returning to the general discussion of ratios, another quite important balance sheet index is the percentage of gross (preferably, net) fixed assets financed by total equity capital (net worth). Financial analysts generally believe that a business should have enough owned capital to at least pay for the fixed investment in property, therefore, 100 percent is the bare minimum thought desirable. Much higher goals are necessary to allow for ownership of nonfixed assets, also. (Another way of viewing the ownership factor in fixed assets is to relate their net value to the amount of fixed liabilities, by dividing the latter into the former. For oil associations a figure higher than three times should be regarded as desirable.)

Another closely related ratio is the percentage of total assets that are financed by equity capital. This, of course, cannot exceed 100 percent and then only in the absence of liabilities of any kind. With some technical exceptions, the higher this index the better, although most credit men probably would be satisfied with a two-thirds proportion.

On this ratio, your local associations run all the way from the severe undercapitalization of 5 percent to the very high figure of 97 percent. One hundred and fifty-six of the oil associations averaged 70 percent for 1951. This is almost identical with the figure Dr. Koller tabulated for 164 petroleum cooperatives located in Minnesota. He showed 65 percent for the 300 Minnesota supply associations of all types.

It should be pointed out that where an association has a funded or long-term debt, such as the debentures discussed earlier, the base of the two foregoing ratios should be changed to include the long-term debt, along with the equity capital. In such an event the term total capitalization is appropriate, it being understood that funded debt in its effect on the balance sheet is to be considered much the same as equity capital.

Balance Sheet Ratios Based on Sales

There are several ways of relating the sales volume to balance sheet figures. First it can be done by the turnover of total capital and second by the turnover of net working capital. Both of these are measures of the relative utilization of capital but they might be aptly classed as somewhat difficult to understand and evaluate. They are not as often used as the third, the turnover of fixed assets. This shows the extent to which property is being put to use as determined by the volume of sales. Naturally an index of this type varies greatly between industries and between sizes of organizations in the same industry. Variance also is brought about when comparing organizations depending upon the price level at which properties were acquired. Old associations might still be operating with cheap facilities, while the newer ones had to acquire property at high price levels. Again, associations part of whose facilities are leased cannot use this ratio to compare with others having owned properties.

A large group of the oil associations studied, showed an average of \$4.90 of sales in 1951 for every dollar invested in fixed property. Often this is referred to as a turnover of 4.9 times. The range is from 2 to above 13. The Minnesota oil associations averaged 9 times for 1950, according to Dr. Koller's survey. But his figures are based on fixed assets after depreciation, while Mr. Lahti used the gross cost of property. This throws the comparison off, although both bases are acceptable, of course.

A fourth way is to appraise the credit and collection policy by determining the turnover of trade receivables. For convenience this can be expressed as the number of days of average sales represented in the closing balance of receivables. I would prefer to use the charge sales only because that method facilitates comparisons between different organizations. The usual way to figure this ratio is on the average credit sales for a whole year. A more reliable indication of the current credit policy is arrived at when the daily sales volume in the extreme latter part of the year is used as the base. This is not often done as it causes more work.

Comment was made previously on the 30 percent rise in receivables between 1951 and 1950 among a large group of Midland associations. The days of sales tied up in receivables had a parallel rise of 32 percent, jumping from 15 to 18 days for oil associations.

A fifth balance sheet-operating ratio is the turnover of inventory. I have already explained at length how this is calculated and have spoken of the implications in the slower turnovers now being experienced. As a point of clarification, let me add here that the 7.7 times annual turnover applicable in 1951 to the oil associations might be somewhat easier to understand if it is related to the days of sales, as in the case of receivables. Thus, the average inventory in 1951 is found to have been large enough to supply customers with products for 40 working days. While this is an improvement over the 45 figure for 1950 it is by no means favorable. A few years back this index was only 35.

OPERATING RATIOS

Sales Ratios

There are a number of operating ratios or percentage relationships to consider, all of which are usually based on sales. First, there is the percentage of gross mark-up, or gross margin. Since the prices charged by supply cooperatives almost invariably parallel the local market level, this ratio does not have quite the same significance for cooperatives that it does for their competitors. In other words, cooperatives could have a fully successful operation if they deliberately cut down their gross margin (not, of course, below an allowance for expenses), providing, of course, that they could at the same time secure capitalization funds from patrons through direct sources. I am very much aware that the present system of mark-ups is the better plan, yet I do think that the gross margin rate in a cooperative should be regarded mainly as an index of purchasing skill.

Other commonly used rates based on sales are those of operating expenses and net savings (or margins). It is also common to show all of the individual items on the operating statement as a percentage of sales. Much good can come from a study of expense trends by months and years and by comparing individual expense ratios with other organizations of like volume. Again let me repeat that cooperatives are formed to operate ultimately at cost, therefore cost efficiency should be one of their top-most aims. Another useful index is the percent of sales represented by the total payroll. This is an excellent indicator of the skillful utilization of manpower. Other similar manpower indexes are the yearly sales per employee and the average compensation per employee.

Special Ratios

Different industry groups have developed special ratios or standards covering their own peculiarities. Perhaps the most prominent of this type for the petroleum industry is the careful check made on the rate of shrinkage in gallons of gasoline. Natural shrinkages from evaporation and temperature changes probably are not subject to much control. But the limits of such changes have been scientifically determined and are well known to you managers.

Variations beyond those limits must be attributed to shorted receipts, to undercharging of customers, to waste, or to other forms of human delinquency, including theft. I was very much surprised to read in Mr. Lahti's report that the 156 oil associations studied by him were aggregating a shrinkage loss of 1.9 percent, or some \$200,000 annually. The larger cooperatives show up with a lesser rate of shrinkage. Does this indicate that smaller tanks have a way of producing greater proportionate errors in gallonage received, or do the smaller associations have inferior supervision?

Volume Indexes

The true trend of business volume (i.e., the number of physical units) has not been revealed in recent years by the recorded sales because of the drastic changes in price levels. Associations interested in knowing the real status of their operating volume could determine it by developing an equated dollar volume index. This could be done for individual commodities by converting the average price applicable in recent years to the price in effect at some earlier year selected as the starting point of the comparison.

Expansion Ratios

Next is an item of particular importance to your associations. It is a consideration of the maximum expansion ratio. Some writers have advanced the theory that no business can expand its sales safely over a period of years more than 10 to 15 times without substantial new capital receipts, in addition to operating margins. Now this was put forward as a general rule. There are at least a few outstanding cooperatives which

have exceeded that rate and still prosper. It is, of course, possible that they may have tapped sufficient new capital.

I suppose it can be categorically stated that any and every business reaches a limit to expansion simply because it is reasonably certain that there must be a ceiling somewhere on its sources of capital. The moral is keep a sharp eye on fast expansion looking particularly toward what could happen to the business if a recession or depression were to come in future years.

OTHER FACTORS IN FINANCIAL MANAGEMENT

We have been discussing some phases of financial management, including the impact of taxes, inflation and expansion; the balancing of capital structures and the conservation of capital; along with analytical factors useful in capital management and planning. There are at least a few more related subjects whose importance demands that they be mentioned, if only in a brief manner. I have in mind mainly the following three items:

1. The use of budgets in the control of expenses and in forecasting financial positions of both short- and long-term durations;
2. The necessity for outside audits and the employment of well-qualified auditors who can act as financial counsellors; and
3. The use of rotating or revolving plans for capital secured in proportion to patronage.

BUDGETING

I want to urge the Midland associations to make greater use of budgeting. It is understood very few of them are now doing so. It is realized, of course, that the managers, particularly of the smaller cooperatives, will claim they have no use for budgets, that they have no one to make them or keep them up, and that in general budgets are difficult to understand and use.

Actually, this is not so. Budgets are not mysterious - they are very simple. The manager of any business - even down to the level of newsboys - uses the principle of budgeting almost every day. He does this whenever he casts a single thought into the future, whether it be tomorrow, next week, next month, or so on. No manager would be worth his salt if he did not actually budget. Usually, however, they do this mentally, or on scraps of paper like the backs of envelopes - some even use their shirt cuffs or tablecloths. Now I like those budgets, but I have a preference for something more systematic.

Budgets can be the best deterrent against the sins of overexpansion that I know of. Ask your auditor to assist you in setting up a budget. Make it a simple one to start with. It may turn out to be one of the best

management moves you ever made. Another good possibility is to ask your directors to appoint a finance committee to work with the manager and auditor on financial planning.

AUDITS AND AUDITORS

On the subject of audits and auditors: Every business, most particularly cooperatives, should have thorough outside audits at least annually. My advice is not to hamstring the auditor by limiting the scope of audit in the hope of saving something on his fee. This is being penny wise and pound foolish. Competent and thorough audits are worth every cent of their cost, not at all merely to prevent wrongdoing but more to receive valuable guidance on financial matters.

The next phase is to pick qualified auditors. Although public accountants are noted for their adaptability, I still say that if you choose an auditor who has had no experience with the peculiarities of cooperative operation you will waste quite a bit of time on his education. From my contacts so far I would say that you are favored with one of the finest groups of auditors I have come across in any part of the country. The zeal they show to assist their cooperative clients is quite outstanding.

I particularly like the kind of audit reports they render, with so much valuable analysis of financial transactions. Again I favor, as they do, the addressing of reports to members and directors, rather than to management alone. This is an enlightened policy that should be more prevalent in other parts of the Nation. Their practice of showing convenient comparison with the prior year's performance is just another evidence of a fine type of service.

ROTATION OF CAPITAL

As to the revolving plan of financing: This is one of the soundest, most ingenious and at the same time fairest plans ever originated in the whole history of financing, in my opinion. But it is a unique device useable only by cooperative organizations. Furthermore, even they can put it to use only when an adequate capital structure has been achieved, and when new capital can be accumulated regularly to pay off the oldest contributions. While a cooperative is expanding, or during any period of rising prices, it may become necessary to curtail or to entirely suspend the capital redemptions which would accomplish the rotation of capital. Members should be properly educated to understand the necessity for any such suspensions.

Whenever possible cooperatives should institute a revolving plan at least to cover the capital secured from patrons in proportion to patronage volume. I say this in the face of the fact that this plan has not met with enthusiastic acceptance in some areas, although I have never been able to quite understand the objections to it. Although seldom if ever done, capital coming from direct contributions could be rotated at least to the extent of new receipts yearly, but this would be a hit-or-miss program of doubtful satisfaction.

It so happens that Midland's member-cooperatives have been growing so fast in the last decade as to preclude any serious thought of capital rotation in other than a few instances. I am sorry that the limitations of time prevent a more extended treatment of capital rotation and the use of budgets.

STUDY FAILURES TO AVOID THEM

In conclusion, let me point out that there is plenty of evidence to indicate that many of the past failures among cooperatives could have been avoided if the participants had applied the principles of sound financing. Cochrane and Elsworth, when members of the Farm Credit Administration staff in Washington, studied the case histories of almost 15,000 farmers' cooperatives which had discontinued operations through 1939.¹

It was revealed that more than one-third of these associations "died" because of difficulties traceable to poor financial planning. A knowledge of how people arrive at the hot place should be valuable for those who are intent on going to heaven. Doesn't this record constitute a powerful plea for more attention to finances? Why not keep a picture of it in your mind? It should be worth a thousand words, as the Chinese say.

¹Cochrane, W. W. and Elsworth, R. H. "Farmers' Cooperative Discontinuances." Farm Credit Administration, U. S. Department of Agriculture, Washington, D. C., Misc. Report 65, June 1943.

